

February 04, 2020

IIFL Securities Limited: Ratings reaffirmed on short term borrowing programme and downgraded to PP-MLD[ICRA]AA- (stable) from PP-MLD[ICRA]AA (stable) on LT – Equity linked debenture programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper programme	1000	-	[ICRA]A1+; reaffirmed and withdrawn
Short Term Bank Lines	650	-	[ICRA]A1+; reaffirmed and withdrawn
LT – Equity linked debenture programme	100	-	PP-MLD[ICRA]AA- (stable); downgraded from PP-MLD[ICRA]AA (stable); and withdrawn
Total	1,750	-	

**Instrument details in Annexure-1*

Rationale

While ICRA used to take a consolidated view of IIFL Finance Limited (erstwhile IIFL Holdings Limited), following the scheme of demerger (effective May 2019), there has been a restructuring, thereby creating three separate entities – India Infoline Finance Limited (lending operations), IIFL Wealth Management Limited (wealth and asset management) and IIFL Securities Limited (capital markets and broking business). The ratings for IIFL Securities Limited (IIFLSL), IIFL Facilities Services Limited, IIFL Insurance Brokers Limited and IIFL Management Services Limited are based on a consolidated view of IIFL Securities Limited (consolidated) (IIFL Securities) and its subsidiaries, given their common senior management team and strong financial and operational synergies.

ICRA has reaffirmed and withdrawn the ratings on short term borrowing programmes of IIFLSL at [ICRA]A1+. ICRA has downgraded and withdrawn the ratings on LT – Equity linked debenture programme of IIFL Securities Limited from PP-MLD[ICRA]AA (stable) to PP-MLD[ICRA]AA- (stable). The revision on ratings is due to the demerger of the business, which results in a separate business for the larger lending book, and wealth management verticals of the erstwhile group. This negates the strong diversification of revenues factored in the rating for the erstwhile group.

The rating favourably considers that the entity as an established player in the broking and investment banking business. It also considers the seniority and experience of the management of the entity. The rating considers the steady profitability of the entity with consistently reported high ROE of over 25% amidst muted capital market conditions (however there was a deterioration in H1FY2020). ICRA notes the augmentation of financial product distribution activities by the entity, which should provide a diversified revenue base with a steady annual stream. ICRA however, takes note of the high gearing at consolidated level (0.47x in H1FY2020 reduced from 1.04x in FY2019 and 1.76x in FY2018). Any upward movement in the consolidated gearing will be a key rating sensitivity. The ratings remain constrained by a reduction in NSE market share of the entity. (1.32% in H1FY2020, 1.76% in FY2019 and 2.00% in FY2018). Additionally, it takes note of the inherent volatility in IIFL Securities' primary business of equity broking, the company's dependence on equity broking income and the intensity of competition in this space.

Key rating drivers and their description

Credit strengths

Established player in the broking and investment banking business, with experienced senior management team: IIFL group started with its broking operations through IIFL Securities Limited in the year 1995. It has served a customer base of ~2,400 crores through a network of about 2,500 points of presence covering branches and business partners over 500 cities in India. The business is overseen by Mr. R Venkataraman (one of the promoters of IIFL group) having an experience of more than 28 years in financial services sector and CEO Mr. Arindham Chanda who has over 19 years of experience in retail broking business.

Steady profitable business, albeit declining in H1FY2020 IIFL Securities has been reporting consistently high ROE of over 25% over the last few years, primarily on the back of strong broking and investment banking revenues and has been paying dividend regularly. However, post the demerger, with IIFL Facilities now being a subsidiary of IIFL Securities, the finance costs and lower broking revenues has resulted in a lower profit after tax of Rs. 62 crore (excluding exceptional items) or a ROE (return on equity) of 15.5% in H1FY2020. ICRA does note that the group intends to gradually decline the debt at IIFL Facilities by selling off the fixed assets, which would improve the profitability, notwithstanding the higher financial products distribution based income.

Augmentation of Financial Product Distribution business:

Historically broking business constituted majority of the revenues of IIFL Securities. However, since FY 2018 the entity has increased its focus on non-broking activities, including financial product distribution and investment banking. The AUM (asset under management) of the entity increased from Rs. 17,800 crore in FY2017 to Rs. 28,600 crore in FY2019. This led to an increase in fee income to Rs. 213.79 crore (24 % of total Income) in FY2019 from 138.83 crore (19% of total income) in FY2017. The technology based platforms developed by IIFL Securities play a key role in facilitating business from self-serviced and partner serviced segments, and provide larger base for cross selling financial products. Diversification of revenues will be a key rating monitorable.

Credit challenges

High gearing at consolidated level, albeit declining in H1FY2020 -

The consolidated net worth stood at Rs. 870.17 crores as on September 30, 2019 compared to Rs. 730.94 crore in FY2019. The increase in net worth was on account of internal accruals of the entity. It should be noted that IIFL Securities had Rs. 41.38 crore of dividend payout in FY2019. However, ICRA does note that historically IIFL Securities had a high consolidated gearing primarily on the borrowings at IIFL Facilities level. The consolidated gearing was 0.47x in H1FY2020 and had reduced from 1.04x in FY2019 (1.76x in FY2018). Total debt of the consolidated entity has reduced from Rs. 759.20 crore in FY2019 to Rs. 405.91 crore in H1FY2020. and the company intends to reduce the debt further. IIFL Facilities Services Limited recorded higher gearing of 7.5x and 9.3x respectively in FY2018 and FY2019. This was on account of higher borrowings backed by fixed assets of the entity. The gearing at IIFL Facilities had reduced to 1.72x in H1FY2020 as the entity had sold one of its assets to a group company which resulted in an exceptional profit of Rs. 101.72 crore. The borrowings at broking entity are required to finance its margining requirement at exchanges and for its margin funding business. The borrowing at IIFL Facilities was against the real estate assets of the company. Any upward movement in the consolidated gearing will be a key rating sensitivity.

Reduction in market share, and inherent risk of capital market business-

The broking volumes of IIFL Securities increased to Rs. 44.13 lakh crore in FY2019 from Rs. 34.83 lakh crore in FY2018 registering a growth of 26.7%. During H1FY2020 IIFL Securities registered a YoY growth of ~0.5% while the industry brokerage volume clocked a growth of 35% YoY (annualized). This resulted in declined NSE market share of the entity.

The NSE market share of IIFL Securities reduced to 1.32% in H1FY2020 from 1.76% in FY2019 and 2.00% in FY2018. Also, with majority of the company's revenues being linked to the inherently volatile capital markets, the company's revenue profile and profitability remain vulnerable to market performance. However, the company has been increasing to diversify by further increasing its focus on distribution business wherein the revenues are linked to AUM, and hence impart stability to the overall earning profile.

Liquidity position: Adequate

The liquidity position of the entity is adequate with unencumbered cash, cash equivalents of Rs. 13 crore as of November 30, 2019 in the form of unencumbered cash, cash equivalents and undrawn fund based bank-lines of Rs. 265 crore from various banks. The total debt due till March 2020 is Rs. 200 crore, against which the company has Rs. 146 crore (cash and equivalents plus unutilized margins placed at exchanges), and further Rs. 265 crore of undrawn bank lines. In addition, the company is also in talks to increase its bank lines.

Rating sensitivities: Not applicable

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA's Rating methodology for entities in broking industry ICRA's Policy on Withdrawal and Suspension of Credit Rating
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of IIFL Securities Limited.

About the company

IIFL Securities was incorporated in 1996 as a broking arm of the IIFL Group. The entity was a part of the IIFL Group with IIFL Holdings Limited (renamed IIFL Finance) holding 100% of the stake in the IIFL Securities as on March 31, 2019. After the scheme of arrangement (effective May 2019), 29.41% of the total equity capital is held by the promoters, 26.51% by Fairfax, 24.75% by institutional investors and 19.33% by other public. The entity was listed on September 20, 2019.

IIFL Securities' net worth stood at Rs. 870.17 crore as on September 30, 2019. It generated a net profit of Rs. 149.08 crore on net operating income of Rs. 293.81 crore in H1 FY2020 compared to a net profit of Rs. 172.10 crore on net operating income of Rs. 683.44 crore in FY2019.

Key financial indicators (consolidated for IIFL Securities Limited)

	FY2018	FY2019	H1 FY2020*
	IND-AS	IND-AS	IND-AS
	Audited	Audited	Unaudited
Brokerage Income (Net)	436.84	441.80	186.65
Net Interest Income	-49.62	-34.14	0.93
Other Non-interest Income (Excl. extraordinary income)	316.97	275.78	106.23
Net Operating Income	704.19	683.44	293.81
Total Operating Expenses	446.10	436.45	210.74
Profit before Tax (Excl. exceptional Income)	273.53	258.08	85.80
Profit after tax [^] *	179.76	172.10	149.08
PAT*/Net Operating Income	38.84%	37.76%	50.74%
Cost-income ratio	63.35%	63.86%	71.73%
Net worth [^]	623.39	730.94	870.17
Gearing	1.76	1.04	0.47
Return on Net Worth*	34.64%	25.41%	37.25%

Amounts in Rs. crore

[^]excluding minority interest

*including exceptional income of Rs. 101.72 crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Instrument	Type	Current Rating (FY2020)		Date and Rating						
		Amount Rated	Amount Outstanding	FY2020	FY2019	FY2018		FY2017		
		(Rs. crore)	(Rs. crore)	04-Feb-20	30-Nov-18	14-Feb-18	31-Aug-17	11-Aug-17	13-Jun-17	05-Oct-16
1	Commercial Paper programme	1,000	NA	[ICRA]A1+; reaffirmed and withdrawn	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
2	Short term bank lines programme	650	NA	[ICRA]A1+; reaffirmed and withdrawn	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	LT - Equity linked debenture	100 [^]	-	PP-MLD[ICRA]AA-(stable); downgraded from PP-MLD[ICRA]AA (stable); and withdrawn	PP-MLD [ICRA]AA (stable)	PP-MLD [ICRA]AA (stable)	PP-MLD [ICRA]AA (stable)	PP-MLD [ICRA]AA (stable)	PP-MLD [ICRA]AA (stable)	PP-MLD [ICRA]AA (stable)

[^]Balance amount unutilised

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Commercial Paper Programme	-	-	7-365 days	1,000	[ICRA]A1+; reaffirmed and withdrawn
NA	Short term bank lines programme	NA	NA	NA	650.00	[ICRA]A1+; reaffirmed and withdrawn
NA [^]	LT -Equity linked debenture	NA	NA	NA	100.00	PP-MLD[ICRA]AA- (stable); downgraded from PP-MLD[ICRA]AA (stable); and withdrawn

[^]Yet to be issued

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
IIFL Securities Limited	Parent	Full Consolidation
IIFL Insurance Brokers Limited	100%	Full Consolidation
IIFL Management Services Limited	100%	Full Consolidation
IIFL Facilities Services Limited	100%	Full Consolidation
IIFL Commodities Limited	100%	Full Consolidation
IIFL Capital Inc.	100%	Full Consolidation
IIFL Wealth UK	100%	Full Consolidation
IIFL Asset Reconstruction Limited	100%	Full Consolidation
Meenakshi Towers LLP	100%	Full Consolidation
Shreyans Foundation LLP	99%	Full Consolidation
IIFL Securities Services IFSC	100%	Full Consolidation

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